Economic Outlook

Irving Trust

Irving Trust Company
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Economic Research &
Planning Division

November 1983

The U.S. economy is in transition. Although the recovery remains solidly based, its pace is shifting from the super-charged growth evident in the second and third quarters to a slower, but more sustainable, one. Real GNP is expected to slow significantly early next year and then grow at 5%-6% annualized rates in the second half of the year. Our forecast calls for a 4.7% rise in real GNP from the fourth quarter of 1983 to the fourth quarter of 1984, following a rise of 6.2% during the comparable 1982-1983 period.

The two prominent interest-sensitive sectors that led the recovery--housing and autos--are now beginning to level off. Housing starts began to revive well in advance of the recession's trough in November 1982. Housing starts rose from 0.87 million units (at an annual rate) in the fourth quarter of 1981 to 1.26 million units in the fourth quarter of 1982 and then to 1.79 million units in the third quarter of 1983. Certainly many of the people who purchased homes during 1983 had been waiting for a considerable period for a break in mortgage rates. From now on, however, the pent-up demand will provide much less support for housing starts. Without a further drop in mortgage rates, housing starts will likely remain on a plateau below the third-quarter level. Although new residential construction can take six to nine months from start to completion, the upward thrust to the economy diminishes as the level of starts holds steady.

The experience of auto sales has been similar to that of housing starts, except that the recovery has been less dramatic. Domestic auto sales totaled 5.0 million units (at an annual rate) in the fourth quarter of 1981 and 6.0 million units in the fourth quarter of 1982; since May of this year, they have hovered around 7.0 million units. With current rates of production in excess of sales, the automakers run a risk of having excessive inventories in the first quarter of 1984. The consequent attempt to bring inventories into line with sales would result in a decline in auto production and would be another factor leading to slower overall economic growth. In addition, more than a third of the real GNP growth in the first nine months of this recovery can be attributed to the shift from inventory liquidation to accumulation, which began in the third quarter. It would be highly unusual for the change in inventories to continue to account for such a large portion of real GNP growth once inventories are rising.

Economic growth will still be reasonably strong in the fourth quarter of this year--retail sales are expected to be excellent during this Christmas season--but the pace of economic activity will likely become subdued in the early part of 1984. We expect that such a development will allow the Federal Reserve to adopt a somewhat easier monetary stance. In view of the continuing weakness and financial strains in the economies of many of our trading partners, declines in U.S. interest rates would certainly be welcomed abroad. These declines would lead to further improvement in housing starts, auto sales, and the overall U.S. economy. As a result, we expect housing starts to total 1.80 million units next year, compared to 1.71 million units this year and 1.06 million units in 1982. Domestic auto sales are expected to total 7.4 million units next year, versus 6.8 million units this year and 5.8 million units in 1982.

Bernard Schoenfeld

Irving Trust

Economic Forecast

Percent Changes at Annual Rates

	Actual*							Forecast	Actual	Forecast	
	1983			1983				1984	1981-	1982-	1983-
	I	II	III	IV	I	II	III	IV	1982	1983	1984
Gross National Product	8.2	13.3	11.6	8.4	7.0	9.9	9.7	10.9	4.0	7.7	9.4
Real GNP	2.6	9.7	7.9	4.8	2.5	5.6	4.9	5.9	-1.9	3.4	5.1
GNP Price Deflator	5.5	3.3	3.4	3.6	4.4	4.1	4.6	4.7	6.0	4.2	4.1

	Actual	Forecast	Actual		Forecast
	1983:III	1983: IV	1981-1982	1982-1983	1983-1984
Consumer Spending	7.6%	10.3%	7.3%	8.5%	9.0%
Durable Goods	9.7	9.6	3.5	13.6	9.5
Nondurable Goods	9.9	11.0	3.7	6.3	7.6
Services	5.3	9.9	11.2	9.0	9.9
Business Capital Spending	15.2	11.5	-1.1	-1.3	11.8
Structures	10.1	7.9	6.4	-7.7	7.2
Equipment	18.6	13.7	-5.7	3.1	14.6
Residential Investment	44.2	5.2	-13.0	43.9	12.7
			1982	1983	1984
Change in Inventories	$11.8b.	$14.0b.	$-24.5b.	$-7.0b.	$15.0b.
Net Exports of Goods and Services	$-25.9b.	$-33.5b.	$17.4b.	$-12.7b.	$-26.0b.
			1981-1982	1982-1983	1983-1984
Government Purchases	11.2%	5.0%	9.0%	6.8%	7.2%
Federal	11.4	8.1	12.9	7.8	10.0
Defense	13.5	10.5	16.5	13.0	12.4
Other	6.1	1.6	5.4	-4.0	3.5
State & Local	11.1	3.0	6.6	6.2	5.4
Corporate Profits Before Tax	26.0F*	39.7*	-23.3	19.2	21.0
Corporate Profits After Tax	27.6F*	37.1*	-20.1	17.2	23.8
Plant and Equipment Expenditures	20.9F	15.4	-1.6	-4.1	10.5
Real Final Sales#	5.1	4.4	-0.7	2.9	4.5
Real Disposable Personal Income	6.7	4.3	0.5	3.0	4.4

Economic Indicators	Recent Data			Actual		Forecast
	July	Aug.	Sept.	1981-1982	1982-1983	1983-1984
Consumer Price Index**	4.8%	4.8%	6.0%	3.9%	3.9%	4.3%
Producer Price Index for Finished Goods**	1.2	4.8	1.2	3.5	1.4	4.3
Industrial Production	26.4	14.4	18.0	-8.2	6.6	9.3
Retail Sales##	0.4	-2.2	1.8	2.7	9.0	9.6
				1982	1983	1984
Auto Sales (millions of units, a.r.)	9.7	8.9	9.2	8.0	9.2	10.0
Housing Starts (millions of units, a.r.)	1.80	1.91	1.65	1.06	1.71	1.80
Unemployment Rate	9.5	9.5	9.3	9.7	9.6	8.2
Merchandise Trade Deficit (a.r.)	$76.3b.	$86.2b.	$69.7b.	$42.7b.	$71.0b.	$85.0b.

Unless noted otherwise, all data are period-to-period percent changes at annual rates, derived from seasonally adjusted data.

November 14, 1983

#GNP less change in inventories, both in real terms.
##Monthly percent changes are not annualized.
*Year-over-year percent changes.
**Annual percent changes are December to December (not seasonally adjusted).
$b. = billions a.r. = annual rate F = Forecast

Economic Outlook

Irving Trust

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Economic Research &
Planning Division

December 1983

This time last year, it was evident that the U.S. economy would be improving during 1983, but the extent of the recovery was underestimated. On all major fronts--real growth, inflation, and unemployment--the performance of the economy has been better than expected. Here's how the economy seems to be shaping up for 1984:

- Real growth will be moderate on average, with real GNP rising 4.7% from the fourth quarter of 1983 to the fourth quarter of 1984. Growth will be slow in the first half of the year, faster in the second half.

- Inflation will remain relatively low, near 4.0%-4.5%. Small increases in unit labor costs and stable oil prices will help restrain inflation, although rising food prices will put upward pressure on overall inflation rates during the latter part of the year.

- The unemployment rate will drop about another percentage point to 7.4% by the fourth quarter of next year.

- Interest rates will remain relatively stable for the time being and then decline during the spring if the economy slows as expected. Later in the year, cyclical pressures will lead to rising interest rates.

In broad terms, these projections characterize an economy behaving in a very normal manner for the second year of recovery. Recoveries that take off at a fast pace usually experience a slowing in real growth during their second year. The major forces that provided a powerful thrust in the initial stages of this recovery--the release of pent-up consumer demand, dramatic recoveries from depressed levels in housing and autos, and a sharp swing from inventory liquidation to accumulation--will not be evident in 1984. Despite the relative slowdown in overall growth next year, however, the consumer will still be in a comparatively favorable position. Real disposable personal income will continue to rise at an above-average pace, helped along by the personal income tax cuts and relatively low inflation. Currently, the large retail chains are having an excellent Christmas selling season and will thus be in a comfortable inventory position at the start of 1984.

The strength in consumer spending has been one of several factors responsible for 1983's record U.S. merchandise trade deficit. Many of today's hot sellers, from Cabbage Patch dolls to VCRs, are made abroad. Of course, the substantial appreciation of the dollar, which as of November 1983 was still 53.9% above the July 1980 level on a trade-weighted basis, has hurt the competitiveness of U.S. exports and given a pricing edge to imports. Continued economic weakness abroad and strains in LDC debt have hurt demand for U.S. capital goods and other exports in 1983 and will continue to affect exports adversely in 1984. Our forecast now calls for a record $104 billion merchandise trade deficit next year versus $73 billion this year and $43 billion in 1982. In sum, 1984 will likely turn out to be a generally favorable year for the U.S. economy, with moderate real growth, low inflation, a declining unemployment rate--but also a disturbingly large trade deficit.

Bernard Schoenfeld

Irving Trust

Economic Forecast

Percent Changes at Annual Rates

	Actual							Forecast	Actual	Forecast	
	1983			1983				1984	1981-	1982-	1983-
	I	II	III	IV	I	II	III	IV	1982	1983	1984
Gross National Product	8.2	13.3	11.2	8.6	7.0	7.9	10.7	12.0	4.0	7.7	9.1
Real GNP	2.6	9.7	7.7	5.1	2.5	3.5	5.9	6.9	-1.9	3.4	4.9
GNP Price Deflator	5.5	3.3	3.3	3.3	4.4	4.2	4.5	4.8	6.0	4.1	4.0

	Actual	Forecast	Actual	Forecast	
	1983:III	1983: IV	1981-1982	1982-1983	1983-1984
Consumer Spending	6.9%	10.1%	7.3%	8.4%	9.1%
Durable Goods	10.2	18.0	3.5	14.2	10.5
Nondurable Goods	7.8	8.3	3.7	5.9	7.4
Services	5.3	9.4	11.2	9.0	10.1
Business Capital Spending	16.9	13.6	-1.1	-1.0	12.7
Structures	8.5	12.5	6.4	-8.0	7.1
Equipment	22.2	14.0	-5.7	3.9	16.1
Residential Investment	41.1	5.2	-13.0	43.5	13.4
			1982	1983	1984
Change in Inventories	$8.7b.	$14.0b.	$-24.5b.	$-7.8b.	$14.0b.
Net Exports of Goods and Services	$-20.2b.	$-32.3b.	$17.4b.	$-11.0b.	$-42.0b.
			1981-1982	1982-1983	1983-1984
Government Purchases	9.7%	6.0%	9.0%	6.7%	7.6%
Federal	7.7	10.6	12.9	7.5	10.9
Defense	5.1	13.1	16.5	12.0	13.7
Other	15.2	4.2	5.4	-2.8	3.8
State & Local	11.0	3.0	6.6	6.2	5.4
Corporate Profits Before Tax	28.1*	40.8*	-23.3	20.0	19.7
Corporate Profits After Tax	21.8*	29.9*	-20.1	14.0	16.8
Plant and Equipment Expenditures	16.2	19.2	-1.6	-4.4	13.1
Real Final Sales#	5.1	4.6	-0.7	2.9	4.4
Real Disposable Personal Income	7.2	5.1	0.5	3.1	5.2

Economic Indicators	Recent Data			Actual	Forecast	
	Aug.	Sept.	Oct.	1981-1982	1982-1983	1983-1984
Consumer Price Index**	4.8%	6.0%	4.8%	3.9%	3.8%	4.3%
Producer Price Index for Finished Goods**	4.8	2.4	3.6	3.5	1.4	4.3
Industrial Production	15.6	16.8	9.6	-8.2	6.6	9.5
Retail Sales##	-1.7	1.4	1.4	2.7	9.1	10.0
				1982	1983	1984
Auto Sales (millions of units, a.r.)	8.9	9.2	9.8	8.0	9.1	10.0
Housing Starts (millions of units, a.r.)	1.90	1.67	1.61	1.06	1.71	1.80
Unemployment Rate	9.5	9.3	8.8	9.7	9.6	7.9
Merchandise Trade Deficit (a.r.)	$86.2b.	$69.7b.	$107.6b.	$42.7b.	$73.0b.	$104.0b.

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December 15, 1983

#GNP less change in inventories, both in real terms.
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$b. = billions a.r. = annual rate F = Forecast

Economic Outlook

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Economic Research & Planning Division

January 1984

The economic recovery will continue this year, but the gains in many areas will be less impressive than in 1983. Real GNP is expected to rise 4.7% from the fourth quarter of 1983 to the fourth quarter of 1984, following a comparable estimated rise of 5.9% last year. Growth will likely slow in the first half of the year, however, and then regain momentum in the second half.

One of the reasons for the expected slowing in real growth--a normal development in the second year of a business recovery--is that last year's postrecession surge in pent-up consumer demand will have diminished. In addition, many families' financial positions were substantially enhanced by the stock market rally beginning in August 1982. If history is any guide, however, increases in the broad market averages are not very impressive in the second year of an economic recovery. As a result, the boost to consumer spending from the stock market will likely be a much less important factor this year than it was in 1983.

One area that has already shown some signs of a slowdown is construction spending, which fell sharply in October and remained flat in November. (The figure for December will probably show a decline because of the unusually harsh weather, which may have been partly responsible as well for the surprisingly small month-to-month increase of 0.1% in December retail sales.) Housing starts in particular seem to have leveled off, bouncing around between 1.65-1.76 million units at an annual rate since last September. With mortgage rates relatively stable, starts are not likely to rise above this range for any sustained period and therefore will not contribute to GNP growth. If interest rates fall in the spring, however, as we expect, housing starts will improve shortly thereafter.

One of the most remarkable developments in this recovery has been the dramatic decline in the unemployment rate, which fell from 10.7% at the recession's trough in November 1982 to 8.2% last December. To put this decline into perspective, the comparable reduction in the unemployment rate in the 1975 recovery (which in most respects was unusually strong) was only nine-tenths of a percentage point. The gain in employment in the first 13 months of both recoveries was exactly the same: 3.8%. The discrepancy arises from the slower growth of the labor force--1.0% in this recovery versus a comparable increase of 2.8% in the 1975 recovery. This slower growth is the result of two factors: a <u>decline</u> in the teenage labor force (16-19 year-olds) and an unusually small rise in the adult female labor force participation rate.

The teenage population has been declining since 1979 and is projected to continue to decline until 1995, with the steepest declines in 1983 (3.1%) and 1984 (3.9%). Since the teenage unemployment rate is very high--currently 20.1%--declines in the teenage population pull down the overall unemployment rate. As a result, with a moderate 2.8% rise in employment expected during the second year of this recovery, the unemployment rate is <u>conservatively</u> estimated to fall to 7.4% by November, a full percentage point lower than a year earlier, versus a comparable decline of two-tenths of a percentage point in the 1975 recovery.

Bernard Schoenfeld

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Economic Forecast

Percent Changes at Annual Rates

	Actual				Forecast				Actual	Forecast	
	1983			1983	1984				1981-	1982-	1983-
	I	II	III	IV	I	II	III	IV	1982	1983	1984
Gross National Product	8.2	13.3	11.5	8.0	7.0	7.8	10.7	12.0	4.0	7.7	9.1
Real GNP	2.6	9.7	7.6	4.0	2.5	3.5	5.9	6.9	-1.9	3.3	4.7
GNP Price Deflator	5.5	3.3	3.6	3.9	4.4	4.2	4.5	4.8	6.0	4.2	4.1

	Actual	Forecast	Actual	Forecast	
	1983:III	1983: IV	1981-1982	1982-1983	1983-1984
Consumer Spending	6.5%	9.5%	7.3%	8.4%	8.9%
Durable Goods	7.6	18.1	3.5	13.9	10.6
Nondurable Goods	7.8	8.0	3.7	5.8	8.0
Services	5.3	8.6	11.2	8.9	9.2
Business Capital Spending	18.8	13.8	-1.1	-0.8	12.8
Structures	11.2	3.4	6.4	-7.8	7.3
Equipment	23.6	20.1	-5.7	4.0	16.1
Residential Investment	47.5	2.9	-13.0	44.2	13.7
			1982	1983	1984
Change in Inventories	$8.5b.	$14.0b.	$-24.5b.	$-7.9b.	$14.0b.
Net Exports of Goods and Services	$-18.3b.	$-30.3b.	$17.4b.	$-10.0b.	$-42.0b.
			1981-1982	1982-1983	1983-1984
Government Purchases	9.0%	5.6%	9.0%	6.5%	8.1%
Federal	6.6	8.8	12.9	7.2	11.5
Defense	3.6	18.7	16.5	12.2	13.8
Other	14.9	-14.3	5.4	-4.0	5.5
State & Local	10.7	3.6	6.6	6.1	5.8
Corporate Profits Before Tax	29.2*	42.1*	-23.3	20.6	19.9
Corporate Profits After Tax	23.7*	32.1*	-20.1	15.0	16.8
Plant and Equipment Expenditures	16.2	15.5	-1.6	-4.6	13.3
Real Final Sales#	5.1	3.3	-0.7	2.8	4.2
Real Disposable Personal Income	6.5	6.1	0.5	3.1	4.9

Economic Indicators	Recent Data			Actual	Forecast	
	Sept.	Oct.	Nov.	1981-1982	1982-1983	1983-1984
Consumer Price Index**	6.0%	4.8%	3.6%	3.9%	3.8%	4.3%
Producer Price Index for Finished Goods**	2.4	3.6	-2.4	3.5	0.6	4.3
Industrial Production	15.6	9.6	8.4	-8.2	6.4	9.6
Retail Sales##	1.4	1.7	1.1	2.7	9.0	9.0
				1982	1983	1984
Auto Sales (millions of units, a.r.)	9.2	9.8	9.5	8.0	9.2	10.0
Housing Starts (millions of units, a.r.)	1.66	1.65	1.76	1.06	1.72	1.80
Unemployment Rate	9.3	8.8	8.4	9.7	9.6	7.9
Merchandise Trade Deficit (a.r.)	$69.7b.	$107.6b.	$88.8b.	$42.7b.	$73.0b.	$104.0b.

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January 13, 1984

#GNP less change in inventories, both in real terms.
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$b. = billions a.r. = annual rate F = Forecast